Supreme Court, U. S.
FILED
MAY 11 1978
MICHAEL RODAK, JR., CLERK

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1977

No. 77-1611

HERCOFORM, INC.

Petitioner

v.

CHICAGO TITLE INSURANCE CO.,
ET AL

Respondents

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

CHARLES W. SMITH, SR.
Attorney for the Petitioner
199 Main Street
Saco, Maine 04072
(207) 282-1527

TABLE OF CONTENTS

	Page
Opinions Below	1
Jurisdiction	1
Question Presented	1
Statutory Provisions	2
Statement of the Case	2
Reasons for Granting the Writ	
A. CERTIORARI SHOULD BE GRANTED TO RESOLVE A CONFLICT AMONG THE CIRCUITS	4
B. THE FIRST CIRCUIT COURT OF APPEALS HAS DECIDED AN IMPORTANT QUESTION OF FEDERAL LAW WHICH HAS NOT BEEN BUT SHOULD BE, SETTLED BY THIS COURT	8
Conclusion	12
Appendex A	13
Appendex B	14
Appendex C	24
Certificate of Service	29

TABLE OF AUTHORITIES

Case Citations

Ault v. Harris, 317 F.Supp. 373 (D. Alaska 1968, Aff'd sub. nom.	6, 9
Ault v. United States, 432 F.2d. 441 9th Cir. 1970) (per curiam order)	6, 9
Baker v. Carr, 369 U.S. 186 (1962)	9
Clearfield Trust v. United States, 318 U.S. 363, 367, 63 S.Ct. 573, 87 L.Ed. 838	9
H. B. Agsten & Sons, Inc. v. Huntington Trust & Savings Bank, 388 F.2d. 156 (4th Cir. 1967), cert denied, 390 U.S. 1025 (1968)	6
Kimbell Food, Inc., Supra, 557 F.2d. 491 (5th Cir. 1977)	6

	Page
Spokane County v. United States 279 U.S. 80, 49 S.Ct. 321, 73 L.Ed. 621 (1929)	4
T. H. Rodgers Lumber Co. v. Apel, 468 F2d. 14 (10th Cir. 1973)	6
United States v. General Douglas MacArthur Senior Village, Inc., 470 F2d. 675 (2nd. Cir 1972)	6
United States v. New Britain, 347 U.S. 81, 74 S Ct. 367 98 L.Ed. 520 (1953)	5
United States v. Security Trust & Savings Bank, 340 U.S. 47, 71 S.Ct. 111, 95 L.Ed. 53 (1950)	5

Statutory Citations

Title 12 -U.S.C.S.- §1701	10
Title 12 -U.S.C.S.- §1701(t)	2, 10
Title 12 -U.S.C.S.- §1710(a)	2, 11
Title 12 -U.S.C.S.- §1710(k)(1)	2, 11
Title 12 -U.S.C.S.- §1715(c)	2, 10
Title 26 -U.S.C.- §6323	5
Title 26 -U.S.C.- §6323(a)(h)(2)	5
Title 28 -U.S.C.- §1254(1)	1
Title 28 -U.S.C.- §1331	3
Title 28 -U.S.C.- §1332	3
Title 28 -U.S.C.- §1391	3
Title 31 -U.S.C.- §191	4

1. OPINIONS BELOW

On February 28, 1977, the United States District Court for the Southern District of Maine issued its Judgment in this case. The ORDER is appended to this Petition as Appendix A. Defendant, Hercoform Incorporated, filed a Notice of Appeal on March 25, 1977. By its Opinion dated January 5, 1978, the United States Court of Appeals For The First Circuit issued an Opinion affirming the District Court's Order. A copy of the Opinion, which has not been reported, appears in Appendix B to this Petition.

2. JURISDICTION

The Opinion and Judgment of the United States Court of Appeals For The First Circuit was entered on January 5, 1978. By Application dated March 16, 1978, the Petitioner sought an Extension of Time within which to file a Petition for a Writ of Certorari. On March 21, 1978, Mr. Justice Brennan signed an Order extending time to file a Petition for a Writ of Certorari until and including May 15, 1978. The jurisdiction of this Court is invoked pursuant to the provisions of Title 28, U.S.C. §1254(1).

3. QUESTION PRESENTED

Whether the choateness doctrine, created by this Court, should be extended to give priority to a federally guaranteed mortgage under the National Housing Act over a mechanics' lien which would otherwise be entitled to priority under State law, thereby unjustly enriching the govern-

ment at the expense of those who furnish labor and materials and increase the value of the subject property.

4. STATUTORY PROVISIONS

National Housing Act, 12 U.S.C.A. §§§1715 (c), 1701(t), 1710(a) and 1710(k)(1). See attached reprinted Appendix "C".

5. STATEMENT OF THE CASE

The facts are by stipulation of the parties and in abbreviated fashion appear as follows:

On September 29, 1971 the Plaintiff, Hercoform Incorporated, a sub-contractor, entered into a contract with Sherred Corp., a general contractor, to supply and erect modular housing units on land of Sherred Village Associates, in Bath, Maine. To help finance the project, Sherred Village Associates, an affiliated corporation with Sherred Corp., on May 2, 1972 mortgaged its premises to the New England Merchants National Bank, the mortgage being insured by the Department of Housing and Urban Development. commonly known as HUD. The Plaintiff, Chicago Title Insurance Company, insured the title.

At the completion of the project substantial sums were owed to Hercoform by way of retainage under the contract and for the current work completed. Hercoform timely filed, in the local registry of deeds, a mechanics' lien to which it was entitled under State law, and on December 20, 1973, after notification to the Bank and HUD, commenced a civil action in the

State Court to enforce its lien claim. While this case was pending, and as a result of the default on payments to the Bank, the Bank assigned its mortgage to HUD in accordance with the terms of its insuring agreement under the National Housing Act. Under State law, Hercoform's lien had priority over the mortgage.

The assignment was without recourse to the Bank except for a warranty that the mortgage assigned was prior to all mechanics' and materialmens' liens filed of record subsequent to the recording of the mortgage. In due course the Bank and the title company initiated a Petition for Declaratory Judgment in the United States District Court, District of Maine, seeking an adjudication as to the priority between the mortgage and the mechanics' lien. Jurisdiction in that Court vested under the provisions of Title 28 U.S.C. §1332 (Diversity of Citizenship), Title 28 U.S.C. §1331 (Federal Question) venue being established under Title 28 U.S.C. §1391. The District Court held that since the mechanics' lien was not choate at the time of the mortgage assignment to HUD, that the lien of the government became superior to the mechanics' lien with the practical result of terminating any liability of the bank or the title company under State law. This decision of the District Court was timely appealed to the United States Court of Appeals For The First Circuit. On January 5, 1978, that Court affirmed the decision of the District Court, saying in essence that while they were sorely tempted to fashion a rule of their own, to do so, they would have to find a substitute formula for the choateness doctrine and therefore joined with the five circuits that had adopted the

choateness doctrine in the non-tax federal lien cases as against the two circuits which had denied application of that doctrine. (See Opinion set forth in Appendix "B").

6. REASONS FOR GRANTING THE WRIT

A. CERTORARI SHOULD BE GRANTED TO RESOLVE A CONFLICT AMONG THE CIRCUITS.

As the Opinion below clearly sets forth (See Appendix "B"), there is a sharp and substantial conflict among the Courts of Appeal on the precise question presented in the case at bar.

The Court below held that Hercoform's lien was not entitled to priority over the Bank's mortgage assigned to HUD since Hercoform's lien was not sufficiently perfected under federal law at the time the mortgage contract was executed. (B-16, 23). The basis of the Court's holding was the application of the federal priority law -- first in time, first in right. In applying the first in time, first in right rule, the Court adopted the "choateness doctrine"--a lien's priority is determined by when it became choate. (B-23).

The choateness doctrine originated in the application of 31 U.S.C. §191 (Rev. Statutes §3466) giving priority to the United States in collection of certain debts from insolvents. The Supreme Court stated that the federal claim would defer only to prior "choate" liens. Spokane County v. United States, 279 U.S. 80, 49 S.Ct. 321, 73 L. Ed. 621 (1929). In order for the lien to be choate, the private lien holder must establish the identity of the lien holder, the property subject

to the lien, and the fixed amount of the lien. United States v. New Britian, 347 U.S. 81, 74 S. Ct. 367, 98 L. Ed. 520 (1953).

In United States v. Security Trust & Savings Bank, 340 U.S. 47, 71 S.Ct. 111, 95 L. Ed. 53 (1950), the Supreme Court applied the choateness doctrine to a priority dispute between federal tax liens and a state lien. Subsequently, the choateness doctrine was applied by some lower federal courts to disputes involving non-tax federal liens. (See cases cited in Footnote 4 of the Opinion Below --Appendix "B").

In response to the harsh results of the application of the choateness doctrine, the Congress, in 1966, amended the lien provisions of the Internal Revenue Code. The Federal Tax Lien Act provided, among other things, that certain private liens could attain priority over federal tax liens. 26 U.S.C. §6323, et seq. Thus, a mechanic's lien would have priority over a federal tax lien if, prior to the recordation of the tax lien, the mechanic's lien had become valid under State law against subsequent purchasers without actual notice and the lienor had commenced work on the project. 26 U.S.C. §6323(a) (h)(2).

Subsequent to the amendment of the Internal Revenue Code by the Tax Lien Act, the lower courts have struggled with the effect, on non-tax federal liens, of the emasculation of the choateness doctrine by the Tax Lien Act. Some Circuits have continued to apply the choateness doctrine in priority disputes involving non-tax federal liens. See, eg.,

United States v. General Douglas MacArthur Senior Village, Inc., 470 F.2d 675 (2nd Cir. 1972); T. H. Rodgers Lumber Co. v. Apel, 468 F.2d 14 (10th Cir. 1973); H. B. Agsten & Sons, Inc. v. Huntington Trust & Savings Bank, 388 F.2d 156 (4th Cir. 1967), cert denied 390 U.S. 1025 (1968). These cases basically limit the effect of the Tax Lien Act to cases involving a dispute between a tax lien and a private lien under state law. The cases argue that Congress could have and should have made further changes in the priority law if it had so desired.

Since the time of the 1966 Tax Lien Act, other Circuit Courts have refused to extend the doctrine of choateness to priority disputes involving non-tax federal liens. See Kimbell Foods, Inc., supra, 557 F.2d 491 (5th Cir. 1977); Ault v. Harris, 317 F.Supp. 373 (D. Alaska 1968, aff'd. sub. nom. Ault v. United States, 432 F. 2d 441 (9th Cir. 1970) (per curiam order). Those cases argue that the choateness doctrine was justifiable in the tax field where the government was an involuntary creditor. However, in the commercial loan area, the government is a voluntary creditor and can take self protection measures before making its investment. Furthermore, since the choateness doctrine has been substantially eroded in the tax lien area by the Tax Lien Act, and since tax collection is an essential governmental function, it would be anomalous to continue applying the choateness doctrine in areas less important to the preservation of the government. See Kimbell Foods, Inc., supra, at 500-03.

The Lower Court in the present case expressed severe doubts about the continued

viability of the choateness doctrine. The Court stated:

> "Choateness has proven a fatal handicap in the race between a mechanics' lienor and a federal lienor. It appears to serve no strong policy, since the federal lienor stands to be enriched by the increase in the property value caused by the work of the mechanics lienor while the latter stands without remedy. Moreover this built in advantage is not necessary to protect the federal investments; the government in mortgage lending and insuring may chose its debtors and set its terms." (App. "B" at 21, 23).

However, the First Circuit Court of Appeals decided not to go against the majority of Circuits which hold that the choateness doctrine is of continued vitality in the non-tax lien area. The Court apparently preferred to have either the Congress of the Supreme Court alter the choateness doctrine and clarify the area for all Circuits.

B. THE FIRST CIRCUIT COURT OF APPEALS HAS DECIDED AN IMPORTANT QUESTION OF FEDERAL LAW WHICH HAS NOT BEEN, BUT SHOULD BE, SETTLED BY THIS COURT.

The issue of whether the doctrine of choateness should be applied in priority disputes involving non-tax federal liens is an important question of federal law which has not been settled by Congress and which should be settled by this Court. This Court has never addressed the issue.

Despite the fact that the First Circuit clearly expressed its sympathy with the plight of mechanic lienors strapped as they are with the judicial expansion of the doctrine of choateness to non-tax federal liens and gave its theoretical support to the minority position that the doctrine should not be thus expanded, the Court regrettably resorted to judicial buck-passing. The Court speculated that falling in with the majority position would more likely attract the interest of Congress which it felt was better equipped to deal with the issue, a consideration which did not deter the Fifth and Ninth Circuits from formulating a workable rule in situations analogous to that of the present case.

As far as Congressional action is concerned, it is an historical fact that the Congress is slow to act and its eventual action, if any, will not aid this Petitioner or the many other mechanic lienors pending such eventuality. Furthermore, historically the Congress has seldom acted as a result of a decision by a lower Court and has waited until this

Court has made a strong and clear pronouncement.

"More significantly, this is a judicially created doctrine whose limitations should be defined by this Court and not by Congress. In the absence of controlling decisions or an Act of Congress to the contrary, it is for the federal courts to fashion the governing rule of law according to their own standards. Clearfield Trust v. United States, 318 U.S. 363, 367, 63 S. Ct. 573, 87 L.Ed. 838." Ault v. Harris, 317 F.Sup., 373, 376 (D. Alaska, 1968), as affirmed in Ault v. United States, 432 F.2d. 441 (9th Cir. 1970).

The judiciary is very well-equipped to answer this question. This Court need only address the very limited question of a priority dispute between a state created mechanic's lien and a mortgage lien assigned to HUD under the National Housing Act. This Court has in the past demonstrated a willingness and an ability to deal with questions having far greater impact upon society and requiring much more of a legislative effort than the deciding of the question presently before this Court. C.f. Baker vs. Carr, 369 U.S. 186 (1962). Furthermore, as hereinbefore pointed out, the facts and policy considerations necessary to support a well-reasoned answering of this question have already been recognized and articulated by the Fifth and Ninth Circuit Courts.

Even the First Circuit Court acknowledged that high priority should be afforded to the reimbursement of those

whose services have enhanced the value of the mortgaged property upon which work was performed (Appendix, Page 21). Likewise, the First Circuit Court was capable of recognizing that providing priority to non-tax federal liens is not necessary to protect the federal investment since the government in mortgage lending and insurance may choose its debtors and set its own terms. (Appendix, Page 22).

Significantly, Congress has already at least impliedly expressed its intention that mechanic's lienors working on HUD insured projects be paid and protected. In the National Housing Act , 12 USCS, §1701, et. seq., the law authorizing and defining HUD's activiities in the current dispute, Congress manifested this intention in several sections: In §1715(c) Congress required that prior to the issuance of any insurance by the secretary of HUD, the principal contractor must file a certificate certifying that laborers and mechanics employed in the construction of the dwellings are being paid not less than the prevailing wage of the locality for similar work. It would be indeed ironic for Congress to take the pains to insure that mechanics are paid an adequate wage in HUD insured construction projects and still intend, under an application of the choateness doctrine, that the same mechanics should go entirely without pay if the owner defaults upon its obligation which would ultimately be assigned to HUD.

In §1701(t) of the National Housing Act, Congress confirmed the national housing goal of a decent home for each

American family and emphasized the capability and resources of private enterprise in realizing this goal. The Congressional goal of utilizing private enterprise in HUD projects is certainly not furthered by an extention of the doctrine of choateness to non-tax federal liens, thereby rendering any investment made by the private sector extremely hazardous.

Sections 1710(a) and 1710(k)(1) both provide that upon the assignment of the obligation to HUD, HUD is to pay the mortgagee for amounts expended by the mortgagee, in addition to the unpaid balance of the principle loan, on such items as taxes, ground rents, and water rates which are liens prior to the mortgage, charges for the maintenance and repair of the mortgaged property, and reasonable payments made for the purpose of protecting, operating, or preserving the mortgaged property. In these sections the Congress has manifested an intention to reimburse those parties responsible for enhancing the value of the mortgaged property. It seems unlikely that the Congress would have intended to rest the reimbursement of these necessary expenditures upon the arbitrary or whimsical decision of the mortgagee to pay them itself prior to assignment, realizing that if the mortgagee did not satisfy these necessary expenses prior to the assignment of the mortgage, the application of the choateness doctrine to non-tax federal liens would preclude the subsequent reimbursement of these mechanics.

CONCLUSION

WHEREFORE, the Petitioner prays that a Writ of Certiorari be granted to resolve a conflict among the Circuits involving an important question of Federal law which equity and justice demand be decided by this Court.

Respectfully submitted,

Charles W. Smith, Sr.

APPENDIX A

UNITED STATES DISTRICT COURT

DISTRICT OF MAINE

SOUTHERN DIVISION

* * * * * * * * * * * * * * * * *

CHICAGO TITLE INSURANCE COMPANY, ET AL,	*	Civil Action
	*	76-56-SD
Plaintiffs	*	
v.	*	
SHERRED VILLAGE ASSOCIATES, ET AL,	*	
Defendants	*	

* * * * * * * * * * * * * * * * *

ORDER ON DECLARATORY JUDGMENT

Hearing having been held on Plaintiffs' complaint for declaratory judgment and upon the stipulation of facts agreed to by the parties, the Court having considered the written briefs and oral arguments presented by the parties, and the Court having made findings of fact and reached conclusions of law, it is hereby

ORDERED, ADJUDGED AND DECLARED that:

The mortgage granted by Sherred Village Associates to New England Merchants National Bank dated May 2, 1972 and recorded in the Sagadahoc Counry Registry of Deeds, Volume 382, Page 312, said mortgage having been assigned to the

Secretary of Housing & Urban Developement by assignment dated December 19, 1974 and recorded in said Registry of Deeds, Book 402, Page 37, is found and declared to be superior to the lien claimed by Hercoform Incorporated in its lien action now pending in the Sagadahoc County Superior Court (Docket #2265), and that said mortgage is entitled to priority over said lien and lien claim.

Costs are awarded to the Plaintiff against Hercoform Incorporated.

/s/ Edward T. Gignoux
United States District
Court Judge

APPENDIX B

United States Court of Appeals
For the First Circuit

No. 77-1157

CHICAGO TITLE INSURANCE COMPANY, et al,

PLAINTIFFS, APPELLEES,

v.

SHERRED VILLAGE ASSOCIATES, et al,

DEFENDANT, APPELLANT.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MAINE

Before

COFFIN, *Chief Judge*,
CAMPBELL, *Circuit Judge*,
WOLLENBERG, *District Judge.**

Charles W. Smith, with whom *Smith, Elliott, Wood & Nelson, P.A.*, was on brief, for appellant.

John W. Philbrick, with whom *Verrill & Dana*, was on brief, for appellees Chicago Title Insurance Company and New England Merchants National Bank.

Thomas G. Wilson, Attorney, Appellate Section, Civil Division, Department of Justice, with whom *Barbara Allen Babcock*, Assistant Attorney General, *Peter Mills*, United States Attorney, and *Ronald R. Glancz*, Attorney, Appellate Section, Civil Division, Department of Justice, were on brief, for appellee Secretary of Housing and Urban Development.

January 5, 1978

COFFIN, *Chief Judge*. Hercoform Incorporated, subcontractor on a housing project in Maine, appeals from a decision that the federal government's mortgage lien has priority over Hercoform's mechanic's lien to proceeds

*Of the Northern District of California, sitting by designation.

from a forthcoming foreclosure. Hercoform contracted to provide and erect prefabricated housing units for the moderate income residential housing project in 1971. In 1972, the developer obtained mortgage financing for the project from the New England Merchants National Bank, whose loan was insured by the Department of Housing and Urban Development pursuant to its authority under Section 236 of the National Housing Act (12 U.S.C. § 1715Z-1(j)). A regulatory agreement between HUD and the developer was recorded along with the mortgage on the day the latter was executed. Chicago Title Insurance Company insured the developer's title in the mortgaged property for the benefit of the Bank.

Hercoform did not record notice of its lien until after its work on the project was completed in 1973. Under the applicable state law there was no need for Hercoform to record the notice before then. On the same day the lien was recorded Hercoform brought suit in state court to enforce its claim.

When the developer defaulted on his payments in 1974, the Bank, pursuant to its rights under the insurance agreement, assigned its mortgage to HUD. In the assignment the Bank warranted to HUD that the mortgage would have priority over all liens recorded after the date on which the mortgage had been filed. Chicago Title insured the Bank's obligations under the warranty.

Under state law Hercoform's lien has priority over the mortgage, since Hercoform's contract was executed before the mortgage was.[1] Seeking to avert the entry of a judgment to that effect in Hercoform's pending state court suit, the Bank and Chicago Title brought suit under the Declaratory Judgment Act (28 U.S.C. § 2201) in the United States District Court for the District of Maine.

[1] 10 M.R.S.A. § 3251; *Saucier* v. *Maine Supply & Garage Co.*, 109 Me. 342, 84 A. 461 (1912).

The relief sought was a declaration that the government's mortgage lien was entitled to priority over Hercoform's mechanic's lien. Hercoform and HUD were named as defendants.

Hercoform moved to dismiss the federal suit on the ground that the plaintiffs lacked standing. The plaintiffs lost their standing, according to Hercoform, when the Bank assigned its mortgage to HUD. The district court, however, denied the motion and, after reviewing the merits, granted the relief which the plaintiffs were seeking.

On appeal Hercoform contends, as it did before the district court, that plaintiffs do not meet the "prudential" rule of standing which requires that the legal rights or interests for which protection is sought be those of the party asserting them, not of a third person. See *Warth* v. *Seldin*, 422 U.S. 490, 499-500 (1975). As a result, though, of the warranty given by the Bank in its assignment to HUD and guaranteed by Chicago Title, plaintiffs do have a legal interest in the outcome of this suit. If Hercoform's lien were held to have priority over HUD's, plaintiff would be liable for breach of warranty and would thereby be legally responsible for any financial loss which HUD might suffer as a result. Consequently, we agree with the district court that plaintiffs did have standing to raise the lien priority issue.

We now turn to the substantive issue. When, as here, there is no governing legislation, federal courts have traditionally applied the federal common law principle that "the first in time is the first in right" to priority disputes involving federal liens.[2] This principle was first enunciated by the Supreme Court in *Rankin* v. *Scott*, 25

[2] See, e.g., *Meyer* v. *United States*, 375 U.S. 233, 236 (1963), *United States* v. *New Britain*, 347 U.S. 81, 85 (1954), *United States* v. *Ringwood Iron Mines, Inc.*, 251 F.2d 145, 146-147 (3rd Cir.) *cert. denied* 356 U.S. 974 (1958), *United States* v. *Latrobe Construction Company*, 246 F.2d 357, 365 (8th Cir., 1957).

U.S. (12 Wheat.) 177 (1827), a case involving a priority dispute between two state-created judgment liens. In resolving the dispute, the Court stated:

> "The principle is believed to be universal, that a prior lien gives a prior claim, which is entitled to prior satisfaction, out of the subject it binds . . . ." *Id.* at 179.

The Supreme Court has since applied the "first in time" rule in a series of cases during the 1950's and early 1960's involving priority disputes between federal tax liens and various kinds of nonfederal liens.[3] With regard to the nonfederal liens, the Court established a federal common law rule to determine when they arose rather than using the dates the liens arose under state law. The Court stated that the determination of when a nonfederal lien "acquired sufficient substance and has become so perfected as to defeat a later-arising . . . federal tax lien" should be governed by federal law. "'Otherwise, a state court could affect the standing of federal liens, contrary to the established doctrine [that the effect of a lien in relation to a provision of federal law for the collection of debts owing the United States is always a federal question].'" *United States* v. *Pioneer American Insurance Company*, 374 U.S. 84, 88-89 (1965), quoting *United States* v. *New Britain*, 347 U.S. 81, 86 (1954); *United States* v. *Security Trust & Savings Bank*, 340 U.S. 47, 49 (1950).

The federal rule adopted by the Court for determining when a nonfederal lien arose for "first in time" purposes was the choateness doctrine; i.e. that a lien's priority was measured from the time it became choate. A lien became choate when the identity of the lienor, the property

[3] See, *e.g.*, *United States* v. *Vermont*, 377 U.S. 351, 358 (1964); *United States* v. *Pioneer American Insurance Company*, 374 U.S. 84, 87 (1963); *United States* v. *Acri*, 348 U.S. 211, 213 (1955); *New Britain, supra*, 347 U.S. at 85.

subject to the lien, and the amount of the lien were all established. *New Britain, supra*, 347 U.S. at 84. Normally, the amount of a lien is not fixed until the debtor has exhausted his opportunities to challenge the amount. Thus, to render his lien choate, the lienor must usually reduce his claim to a judgment. See, *e.g.*, *United States* v. *White Beer Brewing Company*, 350 U.S. 1010 (1956), *United States* v. *Vermont*, 377 U.S. 351, 358-59 (1964). Using the date a lien became choate as the date it arose for "first in time" purposes virtually guaranteed the federal tax lien's priority in order-of-priority disputes, especially those involving mechanics' lienors, who rarely reduced their claims to judgment until after they had completed their work on a project. See, e.g., *White Beer Brewing Company, supra*, 350 U.S. at 1010 (dissenting opinion); *see Kimbell Foods, Inc.* v. *Republic National Bank of Dallas*, 557 F.2d 491, 499 (5th Cir., 1977); W. Plumb, *Federal Liens and Priorities-Agenda For The Next Decade*, 77 Yale L.J. 228, 229-30 (1967).

Following the Supreme Court's application of the "first in time" and "choateness" doctrines in federal tax lien cases, several lower federal courts extended the application of these doctrines to disputes involving non-tax federal liens.[4] In 1966, however, partly in response to the Supreme Court's use of the choateness doctrine, Congress amended the lien provisions of the Internal Revenue Code. One of the primary purposes of the Federal Tax Lien Act of 1966 was to up-date the tax lien laws to be consistent

[4] See, *e.g.*, *United States* v. *Oswald & Hess Co.*, 345 F.2d 886 (3rd Cir., 1965) (Small Business Administration Mortgage Lien); *United States* v. *County of Iowa*, 295 F.2d 257 (7th Cir., 1961) (Reconstruction Finance Corporation mortgage lien); *United States* v. *Roessling*, 280 F.2d 933 (5th Cir., 1960) (mortgage lien under Emergency Relief Appropriation Act of 1935); *Southwest Engine Co.* v. *United States*, 275 F.2d 106 (10th Cir., 1960) (Small Business Administration chattel mortgage lien).

with commercial practice as it had evolved in the states, which through the enactment of mechanics' lien laws had generally given high priority for reimbursement to those whose services enhanced the value of the property upon which they worked. *S. Rep. No.* 1707, 89th Cong., 2nd Sess. (1966), 3 U.S. Code Cong. & Ad. News 3722-25 (1966); *Reports of the Special Committee on Federal Liens,* 83 A.B.A. Rpts. 453-54, 457 (1958) (hereafter, *Special Committee*). Under the amended provisions, a mechanic's lien had priority over a federal tax lien if, prior to the recordation of the tax lien, the mechanic's lien had become valid under state law against subsequent purchasers without actual notice and the lienor had commenced work on the project. 26 U.S.C. §§ 6323(a) and (h)2.

Since the enactment of the 1966 Tax Act, the Circuits have split on the issue of whether the doctrine of choateness should continue to be applied in priority disputes involving non-tax federal liens. The Second, Fourth and Tenth Circuits have continued to apply choateness, primarily on the grounds that: (1) the Tax Act on its face and in its legislative history is limited in scope to federal tax liens, (2) Congress was aware of lower federal court decisions extending choateness to cases involving non-tax federal liens and, therefore, would have acted in these other areas too if it had intended that choateness no longer be applied there, (3) the Tax Act of 1966 is merely the latest in a series of Acts "designed to effect precisely limited expansions of categories of secured creditors protected from secret federal tax liens", and (4) Congress, because of its fact-gathering facilities, is better equipped than the judiciary to gauge the impact of a decision to waive the priority to which federal non-tax liens are generally entitled to now *United States* v. *General Douglas MacArthur Sr. Vil. Inc.*, 470 F.2d 675, 679 (2nd Cir., 1972); *T.H. Rodgers Lumber Company* v. *Apel*, 468 F.2d 14, 17-

20 (10th Cir., 1973); *H.B. Agsten & Sons, Inc.* v. *Huntington Trust & Savings Bank*, 388 F.2d 156, 160 (4th Cir., 1967), *cert. denied*, 390 U.S. 1025 (1968).

The Fifth and Ninth Circuits contend, however, that although the application of choateness may have been justifiable in the field of tax, where the government is an involuntary creditor, its application is not justifiable where the federal government voluntarily extends credit. In the commercial loan area, the government is able to take steps before disbursing funds to protect its investment. Second, since the reliance on choateness has been substantially diminished[5] in the area of tax collection — a governmental function necessary to the very existence of our government and its programs, and also the area in which the doctrine originated — it would be anomalous to continue applying it in areas less central to the preservation of the government. *Kimbell Foods, Inc., supra* 557 F.2d at 500-03; *Ault* v. *Harris*, 317 F. Supp. 373, 374-76 (D. Alaska, 1968), *aff'd sub. nom. Ault* v. *United States*, 432 F.2d 441 (9th Cir. 1970) (per curiam order).

Technically, there being no legislation or Supreme Court opinions governing the non-tax federal lien-mechanics' lien dispute before us, and no circuit precedent, we are free to fashion our own rule. We are sorely tempted to do so. Choateness has proven a fatal handicap in the race between a mechanic's lienor and a federal lienor. It appears to serve no strong policy, since the federal lienor stands to be enriched by the increase in the property value caused by the work of the mechanic's lienor, while the

[5] The lien provisions of the Internal Revenue Code still do not contain priority rules which govern the tax lien's priority with respect to every single kind of nonfederal lien. See 26 U.S.C. § 6323. Therefore, the Supreme Court cases applying the choateness doctrine to federal tax lien — nonfederal lien priority disputes would still seem to be good law in those disputes not governed by the Code.

latter stands without remedy. Moreover, this built-in advantage is not necessary to protect the federal investment; the government in mortgage lending and insuring may choose its debtors and set its terms.

What makes us resist the temptation to announce our own rule is our skepticism that, in this arena of complex relationships intimately affected by both federal and local law, we would make any valuable contribution by adding a further complication. Where the circuits stand, before our decision, at five for choateness and two against, we think that changing the count to six and two may increase the chances of attracting the interest of Congress, if there is sustained demand for reform. While the doctrine was given birth by the Supreme Court, Congress has taken its first bite at reform in the Tax Act of 1966. We cannot avoid feeling that there is much that we do not know about the equities, effects of various rules, and relative ability of the federal and local lienors to protect themselves.[6]

What dissuades us in particular from joining the Fifth and Ninth Circuits is that we would not merely be siding with one camp, making the split in the circuits a bit more even. We would, having decided not to rely on the traditional requirement of choateness in determining the cognizable timing of a mechanic's lien, have to adopt a substitute formula. We would have difficulty in following the Fifth Circuit in *Kimbell Foods, supra,* which applied local law, the Uniform Commercial Code, to a privately

[6] For example, it would seem that decisions such as (1) whether priority of federal liens should be subject to the impermanent policy decisions of state legislatures and (2) to what extent participation by private financial institutions, a primary goal of the National Housing Act, is dependent upon a rule favoring federal liens could be more equitably and intelligently made after Congressional hearings, rather than after a trial between a limited number of litigants.

held secured interest. This device fitted the case admirably, since the U.C.C. is of general, nationwide application, with no quixotic parochial variations. Recourse to the local law governing mechanics' liens, however, would incorporate many local eccentricities.[7] This fact led the Ninth Circuit in *Ault, supra,* to adopt the rule of the Tax Act, *i.e.,* adopting local law except where the mechanic's lienor has not commenced work prior to the recordation of the federal lien. Application of this rule, though, would not only require HUD to concern itself with the varying state laws, but would require contractors to be aware of the possible applicability of two sets of rules.

Were we to carve out our own approach which differed from the court in *Ault,* we would have succeeded only in further complicating a minefield which badly needs some Congressional sapping. In sum, we cannot fault the district court for having chosen the majority rule.

Accordingly, we affirm the district court's decision against the mechanic's lienor because the lien did not become choate before the federal lien arose.[8]

Affirmed.

[7] Depending upon the state involved, a subcontractor's lien may arise when he commences work on the project, when the general contractor commences work, when the subcontractor executes his contract, or the lienor may even be entitled to a superpriority, giving him higher priority than a mortgage lienor regardless of whether the mortgage was recorded before the contractor's work was commenced or his contract executed. W. Plumb, *Federal Liens and Priorities—Agenda for the Next Decade II,* 77 Yale L.J. 605, 677 (1968); *Special Committee, supra,* 83 A.B.A. Rpts. at 457, 494.

[8] Hercoform's reliance on the "circular lien theory" is without merit because there are only two liens involved in this case. *Compare H.B. Agsten & Sons, Inc.* v. *Huntington Trust & Savings Bank,* 388 F.2d 156 (4th Cir. 1967).

Adm. Office, U. S. Courts — Blanchard Press, Inc., Boston, Mass.

APPENDIX C

§1701t. Congressional affirmation of national housing goal

The Congress affirms the national goal, as set forth in section 2 of the Housing Act of 1949 [42 USCS § 1441], of "a decent home and a suitable living environment for every American family."

The Congress finds that this goal has not been fully realized for many of the Nation's lower income families; that this is a matter of grave national concern; and that there exist in the public and private sectors of the economy the resources and capabilities necessary to the full realization of this goal.

The Congress declares that in the administration of those housing programs authorized by this Act which are designed to assist families with incomes so low that they could not otherwise decently house themselves, and of other Government programs designed to assist in the provision of housing for such families, the highest priority and emphasis should be given to meeting the housing needs of those families for which the national goal has not become a reality; and in the carrying out of such programs there should be the fullest practicable utilization of the resources and capabilities of private enterprise and of individual self-help techniques. (Aug. 1, 1968, P.L. 90-448, § 2, 82 Stat. 476.)

1710. Payment of insurance.--(a) In any case in which the mortgagee under a mortgage insured under section 203 [§1709 of this title] shall have foreclosed and

taken possession of the mortgaged property in accordance with regulations of, and within a period to be determined by, the Secretary, or shall, with the consent of the Secretary, have otherwise acquired such property from the mortgagor after default, the mortgagee shall be entitled to receive the benefit of the insurance as hereinafter provided, upon (1) the prompt conveyance to the Secretary of title to the property which meets the requirements of rules and regulations of the Secretary in force at the time the mortgage was insured, and which is evidenced in the manner prescribed by such rules and regulations, and (2) the assignment to him of all claims of the mortgagee against the mortgagor or others, arising out of the mortgage transaction or foreclosure proceedings, except such claims as may have been released with the consent of the Secretary. Upon such conveyance and assignment the obligation of the mortgagee to pay the premium charges for insurance shall cease and the Secretary shall, subject to the cash adjustment hereinafter provided, issue to the mortgagee debentures having a total face value equal to the value of the mortgage and (subject to sub-section (e) (2) a certificate of claim, as hereinafter provided. For the purposes of this subsection, the value of the mortgage shall be determined, in accordance with rules and regulations prescribed by the Secretary, by adding to the amount of the original principal obligation of the mortgage which was unpaid on the date of the institution of foreclosure proceedings, or on the date of the acquisition of the property after default other than by foreclosure, the amount of all payments which have been made by the mortgagee for

taxes, ground rents, and water rates, which are liens prior to the mortgage, special assessments which are noted on the application for insurance or which become liens after the insurance of the mortgage, charges for the administration, operation maintenance and repair of community-owned property or the maintenance and repair of the mortgaged property, the obligation for which arises out of a covenant filed for record and approved by the Secretary prior to the insurance of the mortgage, insurance on the mortgaged property, and any mortgage insurance premiums, and any tax imposed by the United States upon any deed or other instrument by which said property was acquired by the mortgagee and transferred or conveyed to the Secretary, and by deducting from such total amount any amount received on account of the mortgage after either of such dates, and any amount received as rent or other income from the property, less reasonable expenses incurred in handling the property, after either of such dates;...

1710 (k) [j] Notwithstanding any other provision of this section or of section 604 or 904 [§§ 1739, 1750c of this title] and with respect to any debentures issued in exchange for properties conveyed to and accepted by the Secretary after the effective date of the Housing Act of 1959 [Sept. 23, 1959] in accordance with such sections [§§ 1739, 1750c of this title], the Secretary may (1) include in debentures reasonable payments made by the mortgagee with the approval of the Secretary for the purpose of protecting, operating, or preserving the property, and taxes imposed upon any deed or any other instrument by which the property was acquired by the mortgagee and transferred or conveyed to the Secretary;

1715c. Labor standards -- Requirements. --(a) The Secretary [of Housing and Urban Development] shall not insure under section 207 [§1713 of this title] or section 210 of this title or under section 608 of title VI [§1743 of this title] pursuant to any application for insurance filed subsequent to the effective date of this section, or under section 213 of this title [§1715e of this title], or under Title VII [§1747-17471 of this title] pursuant to any application filed subsequent to sixty days after the date of enactment of the Housing Act of 1950 [Apr. 20, 1950], or under section 803 or 810 of title VIII [§§ 1748b, 1748h-2 of this title], or under section 908 of title IX [§1750g of this title], a mortgage or investment which covers property on which there is or is to be located a dwelling or dwellings, or a housing project, the construction of which was or is to be commenced subsequent to such date, unless the principal contractor files a certificate or certificates (at such times, in course of construction or otherwise, as the Secretary [of Housing and Urban Development] may prescribe) certifying that the laborers and mechanics employed in the construction of the dwelling or dwellings or the housing project involved have been paid not less than the wages prevailing in the locality in which the work was performed for the corresponding classes of laborers and mechanics employed on construction of a similar character, as determined by the Secretary of Labor in accordance with the Davis-Bacon Act, as amended (40 U.S.C. 276a--276a-5) [40 §§ 276a--276a-5], prior to the beginning of construction and after the date of the filing of the application for insurance. The provisions of this section shall also apply to the

insurance of any loan or mortgage under section 220 or section 233 [§§1715k, 1715x of this title] which covers property on which there is located a dwelling or dwellings designed principally for residential use for twelve or more families. The provisions of this section shall apply to the insurance under section 221 [§17151 of this title] of any mortgage described in subsection (d)(3) or (d)(4) [§17151 (d)(3) (4)] and (deeming the term "construction" as used in the first sentence of this subsection to mean rehabilitation) of any mortgage described in subsection (h) (1) or section 235(j)(1) [§1715z(j)(1) of this title] which covers property on which there is located a dwelling or dwellings designed principally for residential use for more than eight families; except that compliance with such provisions may be waived by the Secretary--....

CERTIFICATE OF SERVICE

I, Charles W. Smith, a member of the Bar of the Supreme Court of the United States and counsel of record for Hercoform Incorporated, Petitioner herein, hereby certify that on May 11, 1978, pursuant to Rule 33, Rules of the Supreme Court, I served three copies of the foregoing Petition For a Writ of Certorari on each of the parties herein, as follows:

On Chicago Title Insurance Company and New England Merchants National Bank, Respondents herein, by depositing such copies in the United States Post Office, Saco, Maine, with first class postage prepaid, properly addressed to the post office address of John W. Philbrick, Esq., the above-named Respondents counsel of record at Verrill & Dana, Two Canal Plaza, Portland, Maine 04112.

On the Secretary of Housing and Urban Development, Respondent herein, by depositing such copies in the United States Post Office, Saco, Maine, with first class postage prepaid, properly addressed to the post office address of Thomas G. Wilson, Esq., the above-named Respondent's counsel of record at Appellate Sec. Civ. Div., Department of Justice, Washington, D.C. 20530.

On the United States of America, Respondent herein, by depositing such copies in the United States Post Office, Saco, Maine, with first class postage prepaid, properly addressed to the post office address of Wade H. McCree, Solicitor General, the above-named Respondent's counsel of record at Department of Justice, Washington, D.C. 20530.

All parties required to be served have been served.

Dated: May 11, 1978.

Charles W. Smith, Esq.
SMITH, ELLIOTT, WOOD & NELSON, P.A.
199 Main Street
Saco, Maine 04072

Supreme Court, U. S.
FILED
JUN 8 1978
MICHAEL RODAK, JR., CLERK

In the Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-1611

HERCOFORM, INC.
PETITIONER

v.

CHICAGO TITLE INSURANCE CO., ET AL,
RESPONDENTS

On Petition for a Writ of Certiorari to the United States Court of Appeals for the First Circuit

BRIEF FOR CHICAGO TITLE INSURANCE CO. AND NEW ENGLAND MERCHANTS NATIONAL BANK IN OPPOSITION

JOHN W. PHILBRICK, ESQUIRE
VERRILL & DANA
Two Canal Plaza
Portland, ME 04112

Blanchard Press, Inc., Boston, Mass. — Law Printers

TABLE OF CONTENTS

	Page
Proceedings Below	1
Question Presented	2
Statement of the Case	2
Reasons for Denying the Writ	3
A. There Is No Substantial Conflict Among the Circuit Courts.	3
B. The Question Presented by This Record Is a Matter for Congressional, Rather Than Judicial, Resolution.	7
Conclusion	9

TABLE OF AUTHORITIES

Cases

H. B. Agsten and Sons, Inc. v. *Huntington Trust and Savings Bank*, 388 F.2d 156 (4th Cir. 1967) (*en banc*), *cert. denied* 390 U.S. 1025 (1968)	5
Ault v. *Harris*, 317 F. Supp. 373 (D. Alaska 1968), *aff'd sub nom. Ault* v. *United States*, 432 F.2d 441 (9th Cir. 1970)	4, 6
Chicago Title Ins. Co. v. *Sherred Village Associates*, 568 F.2d 217 (1st Cir. 1978)	5
Kimbell Foods, Inc. v. *Republic National Bank*, 557 F.2d 491 (5th Cir. 1977), *cert. granted*, —— U.S. —— (1978)	4, 5, 6, 7
Rankin v. *Scott*, 25 U.S. (12 Wheat.) 177 (1827)	4
T. H. Rogers Lumber Co. v. *Apel*, 468 F.2d 14 (10th Cir. 1972)	5
Saucier v. *Maine Supply & Garage Co.*, 109 Me. 342, 84 Atl. 461 (1912)	6
Spokane County v. *United States*, 279 U.S. 80 (1929)	4

Page

Thorpe Const. Co. v. *Irvine and Co.*, 367 F. Supp. 87 (D. Alaska 1973) 6
United States v. *County of Iowa*, 295 F.2d 257 (7th Cir. 1961) 5
United States v. *Equitable Life Assur. Soc'y*, 384 U.S. 323 (1966) 4
United States v. *General Douglas MacArthur Sr. Village, Inc.*, 470 F.2d 675 (2nd Cir. 1972) 5
United States v. *Latrobe Constr. Co.*, 246 F.2d 357 (8th Cir. 1957), *cert. denied* 355 U.S. 890 5
United States v. *New Britain*, 347 U.S. 81 (1954) 4
United States v. *Oswald and Hess Co.*, 345 F.2d 886 (3rd Cir. 1965) 5
United States v. *Security Trust & Savings Bank*, 340 U.S. 47 (1950) 4

Statutes

26 U.S.C. §6323(b)(7) — 1966 Tax Lien Act 8
31 U.S.C. §191 4

Treatises — Miscellaneous

53 Am. Jur. 2d Mechanics' Liens §247 6
Federal Liens and Priorities — Agenda for the Next Decade II — 77 Yale L.J. 605 (1968) 8

In the Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-1611

HERCOFORM, INC.
PETITIONER

v.

CHICAGO TITLE INSURANCE CO., ET AL,
RESPONDENTS

On Petition for a Writ of Certiorari to the United States Court of Appeals for the First Circuit

---

BRIEF FOR THE RESPONDENTS IN OPPOSITION

Proceedings Below

Respondents concur in the description by the Petitioner of the opinions below and the jurisdiction of this Court (Petition, p. 1), but note that the opinion of the First Circuit Court of Appeals is now reported in 568 F.2d 217 (1978).

Question Presented

Whether a federally guaranteed mortgage under the National Housing Act is entitled to priority over a state-created mechanic's lien unrecorded at the time the federal interest arose.

Statement of the Case

The facts of this case have been stipulated by the parties and appear in the Record Appendix to the Court of Appeals for the First Circuit (hereinafter cited as "App."). Because the Petition fails to set forth some important factual material, Respondents would summarize the case as follows:

On September 29, 1971, Petitioner, a subcontractor, entered into a contract with a general contractor to furnish and erect pre-fabricated modular housing units for a moderate income residential housing project. On May 2, 1972, the owner of the property to be developed granted a construction mortgage of its premises to New England Merchants National Bank (hereinafter "Bank"), the mortgage being insured by the Department of Housing and Urban Development (hereinafter "HUD"); both the mortgage and the Regulatory Agreement between HUD and the owner were recorded on that date in the appropriate Registry of Deeds (App., pp. 15, 16, 22-35). Among other indicia of HUD involvement in the transaction, the Regulatory Agreement set forth conditions under which the mortgage could be assigned to HUD after default (App., p. 33).

Over eighteen months after the recordation of the mortgage and Regulatory Agreement, the Petitioner filed a mechanic's lien on December 20, 1973, and simultaneously instituted a civil action to enforce its lien in the State

Court (App., pp. 8, 36-39). Thereafter, as a result of mortgage defaults, the Bank duly assigned its mortgage to HUD in accordance with the Regulatory Agreement (App., p. 19), warranting that the mortgage had priority over all liens or encumbrances (App., p. 40).

Respondent, Chicago Title Insurance Company, insurer of the title to the premises, and the Bank later brought a declaratory judgment action in the United States District Court claiming entitlement to a judgment that Petitioner's lien claim was inferior to the mortgage interest. Petitioner timely appealed the District Court's ruling that the federally insured mortgage was entitled to priority, and has sought a writ of certiorari to review the First Circuit Court's judgment of affirmance.

Reasons for Denying the Writ

A. There Is No Substantial Conflict Among the Circuit Courts

The Court of Appeals, in affirming the District Court judgment declaring the priority of the federal lien, chose not to depart from the rule followed by the clear majority of Federal Court opinions: inchoate state liens cannot prevail over federal liens and mortgages. While recognizing that there had recently been some departure from the formerly unanimous view that the choateness doctrine applied to disputes between a federal non-tax lien and a state-created lien, the Court was understandably unwilling to depart further from a general rule of universal application in order to deal with the vagaries of local perfection requirements of state liens such as mechanic's liens. 568 F.2d at 221.

Petitioner argues (Pet., p. 4) that a "sharp and substantial" conflict exists between seven circuits applying

the choateness doctrine to non-tax federal liens (see cases cited at p. 5, *infra*) and the two circuits which are said to have rejected the doctrine. *See Kimbell Foods, Inc.* v. *Republic National Bank*, 557 F.2d 491 (5th Cir. 1977) *cert. granted*, —— U.S. —— (1978) and *Ault* v. *Harris*, 317 F.Supp. 373 (D. Alaska 1968), *aff'd sub nom. Ault* v. *United States*, 432 F.2d 441 (9th Cir. 1970). An examination of these decisions, viewed against the historical development of the doctrine and the facts of this case, shows that there is no such conflict.

It is firmly established that federal law governs a dispute involving the priority of a federal debt. *See, e.g., United States* v. *Equitable Life Assur. Soc'y*, 384 U.S. 323, 327-328 (1966); *United States* v. *Security Trust & Savings Bank*, 340 U.S. 47, 49 (1950). The federal test is "first in time, first in right." *See, e.g., United States* v. *New Britain*, 347 U.S. 81 (1954); *Rankin* v. *Scott*, 25 U.S. (12 Wheat) 177, 179 (1827). In order to establish which competing lien is "first in time," federal law requires that the state-created lien be "choate" at the time the federal lien attaches. *United States* v. *New Britain, supra*, 347 U.S. at 86. A "choate" lien has been defined as one in which the lienor, the property subject to the lien, and the fixed amount of the lien are firmly established. *United States* v. *New Britain, supra.*

The "choateness" doctrine evolved from the application of 31 U.S.C. § 191, which accorded certain federal priorities in claims against insolvents. This Court held nearly fifty years ago that only "choate" liens would be entitled to priority over federal claims under that statute. *Spokane County* v. *United States*, 279 U.S. 80 (1929). In 1950 this Court extended the choateness concept beyond the insolvency statute and applied it in resolving priorities between a federal tax lien and a state-created lien against property of a solvent debtor. *United States* v. *Security Trust and Savings Bank*, 340 U.S. 47 (1950). In the ensuing twenty-eight years, seven courts of appeals have applied the choateness test to disputes between federal non-tax liens and state liens. *Chicago Title Ins. Co.* v. *Sherred Village Associates*, 568 F.2d 217 (1st Cir. 1978); *United States* v. *General Douglas MacArthur Sr. Village, Inc.*, 470 F.2d 675 (2nd Cir. 1972); *T.H. Rogers Lumber Co.* v. *Apel*, 468 F.2d 14 (10th Cir. 1972); *H.B. Agsten and Sons, Inc.* v. *Huntington Trust and Savings Bank*, 388 F.2d 156 (4th Cir. 1967) (*en banc*), *cert. denied* 390 U.S. 1025 (1968); *United States* v. *Oswald and Hess Co.*, 345 F.2d 886 (3rd Cir. 1965); *United States* v. *County of Iowa*, 295 F.2d 257 (7th Cir. 1961); *United States* v. *Latrobe Construction Co.*, 246 F.2d 357 (8th Cir. 1957), *cert. denied* 355 U.S. 890. Only two circuit court opinions can be viewed as having deviated from this well established rule, and neither case appears to be in conflict with the result reached by the First Circuit in the instant case.

In *Kimbell Foods, Inc.* v. *Republic National Bank*, 557 F.2d 491 (5th Cir. 1977), *cert. granted* U.S. , the Court held that a filing under the Uniform Code was entitled to priority over a subsequent federal mortgage, notwithstanding the fact that the state lien had not been reduced to judgment at the time the federal mortgage arose; however, it specifically excluded from the scope of its decision and rationale any applicability to mechanic's lien cases, such as the one at bar. In much the same manner as Judge Coffin in this case stated the First Circuit's unwillingness to fashion a new and different rule of priority covering varied and parochial methods of perfecting mechanic's liens (568 F.2d at 222), the *Kimbell* Court stated:

> Other types of state liens — for taxes, for mechanics and materialmen, or for certain types of secured loans — present problems that we leave for another day. First, the manner of perfection of those liens is

> diverse — creating havoc with a nationwide program — and may not provide notice sufficient for federal entities to ascertain their existence before granting loans. Second, consideration of these loans for qualification under the federal "first in time, first in right" rule is complicated by the fact that several states, including Texas, either provide special priorities for the liens . . . or allow subsequently perfected liens to relate back to the date the debt was incurred . . . . *Kimbell Foods, Inc.* v. *Republic National Bank,* 557 F.2d at 503, n.15.

The Fifth Circuit, having thus expressly refused to decide the issue presented by this record, cannot be said to be in conflict with the First Circuit.

The Ninth Circuit has addressed this issue only by a *per curiam* affirmance of a district court opinion in *Ault* v. *Harris,* 317 F. Supp. 373 (D. Alaska 1968), *aff'd sub nom Ault* v. *United States,* 432 F.2d 441 (1970). More recently, however, a subsequent decision by Judge Plummer, author of the *Ault* opinion, indicates an intent to limit *Ault* to its facts for reasons fully applicable to this case. *See Thorpe Const. Co.* v. *Irvine and Co.,* 367 F. Supp. 87 (D. Alaska 1973). Just as acceptance of an unusual provision of Alaska lien law would have been necessary to defeat federal priority in *Thorpe,* acceptance of an unusual provision of Maine lien law is necessary to create a "first-in-time" priority in favor of the Petitioner in this case. *Compare Saucier* v. *Maine Supply & Garage Co.,* 109 Me. 342, 84 Atl. 461 (1912) (lien relates back to execution of contract) *with* cases collected in Am. Jur. 2d Mechanics' Liens, §247 (lien relates back to furnishing of first labor materials). Indeed, without both this peculiar provision of Maine law *and* the rejection of the "choateness" doctrine applied in at least seven circuits, the federal interest in this case, which

arose at the recordation of the Regulatory Agreement (*Kimbell Foods, supra,* at 503), would have unquestionable priority over the subsequently recorded lien, in the absence of evidence that construction commenced prior to the Regulatory Agreement.

In summary, the Fifth Circuit's express refusal to decide the issue prescribed by this case and the Ninth Circuit's 1970 *per curiam* affirmance of a case that has been limited to its facts hardly creates a conflict with the opinion below that requires resolution by this Court at this time.

There simply is no "sharp and substantial" conflict among the circuits on the issues presented by this record.

B. The Question Presented By This Record Is a Matter for Congressional, Rather Than Judicial, Resolution

The choateness doctrine, applied by this Court to settle disputes involving federal tax liens and by the lower federal courts to disputes involving federal non-tax liens, represents a rule of federal common law by which priorities between state and federal liens may be easily and predictably decided. Because of its universality of application and consistency of result, the rule can be easily applied in a variety of circumstances. If it is to be modified (or abandoned, as petitioner urges), and a new federal common law rule fashioned by this Court to replace it, the first judicial steps in modifying the "choateness" doctrine should be taken in a case in which any new rule affecting diverse federal interests can be narrow and consistent in its application. If the choateness doctrine applied in seven circuits is to be judicially reexamined, it should be done in a situation such as that presented in *Kimbell Foods, supra,* where the universally adopted Uniform Commercial Code provides a commercially tolerable and broadly recognized

definition of the time when a security interest attaches. In these circumstances, there may exist a rational and finite judicially-created alternative to the choateness doctrine.

Where mechanics' lien claims on projects subject to federal liens are concerned, however, any proposed revision or abandonment of the choateness doctrine should be legislatively investigated. State-created mechanics' liens arise in many different ways and at many different times; there is no uniform rule which can be adopted as federal common law. *See* W. Plumb, *Federal Liens and Priorities — Agenda for the Next Decade II*, 77 Yale L.J. 605, 677 (1968). As noted by the First Circuit (568 F.2d at 221-22), the courts are ill-equipped to determine the impact of adopting a new rule of priority upon such varied factual and legal settings; there is good reason to defer to the Congress the reform, if any is needed, of the rules regulating priorities of federal interests over state-created mechanics liens. Congress has the capacity to hold hearings, seek expert advice, and create policy respecting the priorities of demands on the national treasury. Thus far, against the experience of the decisional law upholding applicability of the choateness doctrine to federal non-tax liens, Congress has acceded to those decisions and has not legislatively altered the result reached by the federal courts. If Congress determines that the result reached by the First Circuit in following settled law ought to be examined, it has the power and resources to investigate and to resolve the complex problems of lien priorities in federally insured housing projects under construction in each of the fifty states. Congress has already acted to reshape priorities between federal tax liens and certain state mechanics liens under very limited circumstances. 1966 Tax Lien Act, 26 USC §6323(b)(7). But until Congress acts, this Court should not intercede in a field where no substantial conflict among

the circuits exists and where the Court does not have the investigative resources to resolve what is essentially a legislative problem of governmental priorities.

Conclusion

Because there is no real conflict among the Circuit Courts of Appeal and because the Congress can best determine the necessity for, and scope of, any changes in the existing law establishing priorities between federal interests and state mechanics' liens, this Court should deny the petition for a writ of certiorari.

Dated: June 1, 1978

Respectfully submitted,

JOHN W. PHILBRICK
Attorney for Respondents
Chicago Title Insurance Co. and
New England Merchants National
Bank

VERRILL & DANA
Two Canal Plaza
Portland, ME 04112
Tel. 207 774-4573

Supreme Court, U. S.
FILED
JUN 14 1978
MICHAEL RODAK, JR., CLERK

No. 77-1611

In the Supreme Court of the United States

OCTOBER TERM, 1977

HERCOFORM INCORPORATED, PETITIONER

v.

CHICAGO TITLE INSURANCE COMPANY, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

MEMORANDUM FOR THE FEDERAL RESPONDENT

WADE H. MCCREE, JR.,
Solicitor General,
Department of Justice,
Washington, D.C. 20530.

In the Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-1611

HERCOFORM INCORPORATED, PETITIONER

v.

CHICAGO TITLE INSURANCE COMPANY, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

MEMORANDUM FOR THE FEDERAL RESPONDENT

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 15-23) is reported at 568 F. 2d 217. The oral opinion of the district court (App., *infra,* pp. 1a-4a) is not reported.

JURISDICTION

The judgment of the court of appeals was entered on January 5, 1978. On March 21, 1978, Mr. Justice Brennan extended the time within which to file a petition for a writ of certiorari to and including May 15, 1978. The petition was filed on May 11, 1978. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether a private mechanic's lien that has not become choate before a federal lien attaches takes precedence over the federal lien.

STATEMENT

1. In September 1971 petitioner contracted with Sherred Corp. to fabricate, deliver, and erect prefabricated housing units for the Sherred Village project in Bath, Maine (C.A. App. 15-17).[1]

In May 1972 the project's owner and developer, Sherred Village Associates, obtained a $3.98 million mortgage loan, from New England Merchants National Bank, on the Bath property (C.A. App. 22-29). This loan was insured by the Department of Housing and Urban Development (HUD) pursuant to Section 236 of the National Housing Act, as added, 82 Stat. 498, and amended, 12 U.S.C. 1715z-1.[2] The mortgage and a regulatory agreement between HUD and Sherred Village Associates were recorded on May 2, 1972, with the appropriate county office (C.A. App. 16, 29, 35). Chicago Title Insurance Co. provided title insurance for the benefit of the Bank; among the risks insured against were liens existing as of the date of the mortgage (C.A. App. 16).

Petitioner completed work in late 1973, filed a $440,986.03 mechanic's lien against the property on December 20, 1973, and on the same date filed suit in the Sagadahoc County Superior Court to enforce its lien (C.A. App. 18).

On December 19, 1974, while that case was pending and after Sherred Village Associates had defaulted on its mortgage payments, the Bank assigned its interest in the mortgage to HUD; this assignment was appropriately recorded. The bank warranted to HUD that the mortgage

[1]"C.A. App." refers to the Appendix in the court of appeals.

[2]Section 236 authorizes HUD to insure mortgages on rental developments of five or more units for "lower" income families or elderly or handicapped persons.

assigned was prior to all mechanics' and materialmen's liens filed after the recording of the mortgage in May 1972 (C.A. App. 40).[3]

2. In April 1976 Chicago Title and the Bank brought a declaratory judgment action in the United States District Court for the District of Maine, seeking a determination that petitioner's mechanic's lien is inchoate and junior to the mortgage insured under Section 236 (C.A. App. 4-8). Petitioner argued in response that Maine law should be applied, and that under Maine law its lien was perfected and obtained priority as of the date the construction contract was signed, September 29, 1971.

The district court concluded that federal law should be applied, and that, under the federal rule, the lien "first in time" should be "first in right" (App., *infra*, p. 2a). It then determined that petitioner's mechanic's lien could not be first in time because it was not "choate" either at the time the mortgage was first recorded or at the time it was assigned to HUD; the lien was not choate because it was still subject to judicial contest in proceedings pending in state court (App., *infra*, pp. 2a-3a). The court concluded that the HUD-insured mortgage therefore was entitled to priority (App., *infra*, p. 4a; Pet. App. 13-14).

3. The court of appeals affirmed (Pet. App. 15-23). It observed that since the enactment in 1966 of amendments limiting the choateness doctrine as applied to federal tax liens, see 26 U.S.C. 6323, "the Circuits have split on the issue of whether the doctrine of choateness should continue to be applied in priority disputes involving non-tax federal liens" (Pet. App. 20) and that "[t]echnically, there

[3]We are informed by HUD that HUD has not foreclosed on the mortgage, and that Sherred Village Associates remains the owner and operator of the mortgaged property.

being no legislation or Supreme Court opinions governing the non-tax federal lien-mechanics' lien dispute * * *, we are free to fashion our own rule" (*id.* at 21). But the court concluded that it would "resist the temptation to announce our own rule" because of "skepticism that, in this arena of complex relationships intimately affected by both federal and local law, we would make any valuable contribution by adding a further complication" (*id.* at 22). It determined that any "substitute formula" that it could devise would be unsatisfactory, particularly because the lien at issue was a mechanic's lien to which the Uniform Commercial Code does not apply. Applying local law as a substitute would "incorporate many local eccentricities," while applying the Federal Tax Lien Act of 1966 would "require contractors to be aware of the possible applicability of two sets of rules," for those amendments do not uniformly follow state law[4] (Pet. App. 22-23).

DISCUSSION

This case raises the issue whether a private lien that has not become "choate" before a federal lien attaches can take precedence over the federal lien. This question is before the Court in *Kimbell Foods, Inc.* v. *Republic National Bank*, 557 F. 2d 491 (C.A. 5), certiorari granted *sub nom. United States* v. *Kimbell Foods, Inc.*, No. 77-1359, May 15, 1978. We accordingly suggest that the Court defer consideration of the petition in this case pending the disposition of *Kimbell*. If the Court agrees with our argument in *Kimbell* that a private lien achieves priority against a federal non-tax lien only from the date

[4]26 U.S.C. 6323(a) and (h)(2) provide that a mechanic's lien achieves priority for purposes of comparison with tax liens "on the earliest date such lien becomes valid under local law against subsequent purchasers without actual notice, but not before [the mechanic's lienor] begins to furnish the services, labor or materials."

it becomes "choate," it would follow that the decision of the court of appeals here is correct. In any other event, the proper disposition of the present case would depend on the Court's rationale in *Kimbell*.

This case also is related to *United States* v. *Crittenden*, 563 F. 2d 678 (C.A. 5), petition for certiorari pending, No. 77-1644, which involves a loan, made directly by a federal agency, that is in competition with a repairman's lien. The repairman's lien was neither "choate" nor perfected under any other theory at the time the federal lien attached. *Crittenden* therefore presents the question whether a private lien can be accorded a "super-priority" over a federal lien. Our petition in *Crittenden* observed that the Court might disagree with our contentions concerning the choateness doctrine and still decline to accord "super-priority" to liens that come into existence, under any test, only after the federal lien attaches.[5]

The present case does not involve a question of super-priority; petitioner apparently asks this Court to apply Maine law, which would give petitioner an early date for perfection of its lien but would not grant any form of priority over liens that were perfected before that time. But because this case, like *Crittenden*, involves a claim by a mechanic or repairman who has worked on an item of personal or real property, the Court may wish to defer consideration of this petition until it has decided *Crittenden*.[6]

[5]We have furnished copies of the petitions in *Kimbell* and *Crittenden* to counsel for the private parties in this case.

[6]Our petition in *Crittenden* asks the Court to set that case for consideration in tandem with *Kimbell*, so that it may consider claims of both ordinary and super-priority. Because the mechanic's lien here is entitled under state law to early but not super-priorty, this case apparently does not present any issue that would not be before the Court in *Kimbell* or *Crittenden*.

CONCLUSION

The Court should defer consideration of the present petition until it has disposed of *Kimbell* and *Crittenden*.

Respectfully submitted.

WADE H. MCCREE, JR.,
Solicitor General.

JUNE 1978.

DOJ-1978-06

APPENDIX

UNITED STATES DISTRICT COURT
DISTRICT OF MAINE
SOUTHERN DIVISION

CHICAGO TITLE INSURANCE COMPANY, ET AL.,

PLAINTIFFS

v.

SHERRED VILLAGE ASSOCIATES, ET AL.,

DEFENDANTS

CIVIL NO. 76-56-SD

BENCH RULING OF THE COURT AT THE CONCLUSION OF ORAL ARGUMENTS IN THE ABOVE-ENTITLED ACTION

Pursuant to notice, hearing was had in the above-entitled matter before Honorable Edward T. Gignoux, Judge, United States District Court, District of Maine, at the United States Courthouse, Portland, Maine, on Wednesday, February 16, 1977. At the conclusion of oral argument of counsel, the Court ruled from the bench as follows:

THE COURT: Counsel, thank you all very much. As previously noted, the Court has reviewed the record and the briefs submitted by counsel and has read the *Bellegarde Custom Kitchens* case and the significant cases cited in the briefs. It is prepared to rule at this time.

Plaintiffs seek a declaratory judgment as to the priority between the real estate mortgage executed and recorded, together with a HUD regulatory agreement, on May 2d 1972, and subsequently assigned to the Secretary of HUD on December 19, 1974, recorded December 30, 1974, and a mechanic's lien asserted by the defendant Hercoform,

Incorporated, arising as a result of materials and labor furnished in the construction of housing upon the real estate in question. The facts have been stipulated and the Court finds the facts as stipulated.

The legal issues have been well briefed and orally argued by able counsel. The Court is persuaded that the present case is in all respects save one controlled by the prior decision of this Court in *Bellegarde Custom Kitchens v. Select-A-Home, Incorporated* and *LaPointe Bros., Inc. v. Chabot*, 385 F. Supp. 318 (D. Me. 1974). As this Court concluded in that case, federal law governs the priority of liens when a debt owing the federal government or an agency of the federal government is involved. The federal rule for determining the relative priority between a federal lien and a state-created lien, in the absence of a controlling federal statute, is "first in time, first in right." In applying this federal rule, the Supreme Court of the United States has consistently held that in order for a non-federal lien to be entitled to priority over a federal lien, the non-federal lien must be choate at the time the federal lien arises. The authorities have further established that a non-federal lien is choate only if the identity of the lienor, the property subject to the lien and the amount of the lien are established, and that a non-federal lien is not choate until the claim is final and not subject to a judicial contest as to its validity or amount. Furthermore, the authorities are clear that the determination of whether a non-federal lien is choate is to be made in accordance with federal law, even though the application of state law might bring about a different result.

On the record here presented, there can be no question but that if, as in *Bellegarde*, the mortgage in question were a direct federal mortgage, the federal lien would be entitled to priority over the Hercoform lien. Hercoform's

lien was not choate under applicable federal law either at the time the mortgage and regulatory agreement were executed and recorded or at the time the mortgage was assigned to HUD. As a matter of fact, the Hercoform lien is not yet choate under the federal definition, inasmuch as the amount of the lien has not yet been established. Indeed, the claim itself is still subject to judicial contest in proceedings pending in the courts of the State of Maine.

The only question presented by this case which was not previously ruled upon by this Court in *Bellegarde Custom Kitchens* is whether the fact that the mortgage here in question was not a direct federal mortgage but a federally-insured mortgage is a controlling distinction. The authorities are clear, however, that the result must be the same where, as in the present case, the mortgage, although taken by a private lender, was insured by a federal agency and subject to the terms of a regulatory agreement which disclosed to the world the possibility that in the event of default an assignment to the federal agency would ensue and a federal lien be asserted. *See, e.g., United States v. Eklund*, 369 F. Supp. 1052 (S.D. Ill. 1974); *Kimbell Foods, Inc. v. Republic National Bank of Dallas*, 401 F. Supp. 316 (N.D. Texas 1975); *J.S. Purcell Lumber Corp. v. Hanson*, 405 F. Supp. 1130 (E.D. Va. 1975); *United States v. Chester Heights Association*, 406 F. Supp. 600 (D.S.C. 1975).

The defendant Hercoform in the instant case places great reliance upon *H. B. Agsten & Sons, Inc. v. Huntington Trust & Savings Bank*, 388 F. 2d 156 (4th Cir. 1967). A careful analysis of the factual situation presented in that case, as well as the law applied, persuades this Court, however, that it is plainly distinguishable. In *Agsten*, the court was confronted with a circular lien situation. The court broke the circle in the manner which seemed to it most fair to the various parties

concerned. In the present instance, no circular lien problem is presented. The issue as agreed by the parties is as to the priority as between the federal government mortgage lien and the state-created mechanics lien.

The defendant Hercoform also argues that the enactment by Congress of the Federal Tax Lien Act of 1966, which subordinated federal tax liens to various state security interests, including state mechanics liens, evinces a federal policy to subordinate all federal liens to liens created by state law. As defendant's counsel correctly points out, two circuit courts have accepted this line of reasoning. It has, however, been rejected by other circuit courts and by this Court in *Bellegarde Custom Kitchens.* The Court is not persuaded that the views there expressed should be modified at this time.

The Court holds that the lien of the mortgage dated May 2d, 1972, given to New England Merchants National Bank and assigned to the Secretary of Housing and Urban Development on December 19, 1974, is entitled to priority over the mechanics lien asserted by the defendant Hercoform, Incorporated. The declaratory judgment requested in the complaint will be entered.